



Foreign Agricultural Service

GAIN Report

Global Agriculture Information Network

Required Report - public distribution

Date: 3/6/2000

GAIN Report #AJ0002

Azerbaijan, Republic of

Tobacco and Products

Annual Report

2000

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Report Highlights:

Tobacco and cigarette production in Azerbaijan has been greatly diminished in recent years as a result of the changing economy. Producers are moving into other crops where income is more assured. The main cigarette plant in the country has undergone at least three ownership changes since 1997.

Includes PSD changes: Yes
Includes Trade Matrix: No
Annual Report
Ankara [TU1], AJ

Tobacco

The tobacco sector in Azerbaijan has seen a dramatic fall-off in leaf production due to a combination of an overvalued exchange rate for the Azeri manat and the bottoming out of their only market in Russia. Tobacco farmers (mostly oriental leaf) have begun to shift production away from this undependable cash crop to more tradable fruits and vegetables. Azerbaijan geared up tobacco production in the last years of the Soviet Union, at one point producing 62,000 metric tons (mt), but has been averaging between 8-15,000 mt per annum since independence. Russia has been the primary export market for the lesser quality Azeri tobaccos, which is only suitable for inexpensive Russian-style cigarettes.

The Russian economic crisis of 1998 severely dried up demand at the same time the overvalued Azeri manat kept and keeps Azeri leaf from competing with the large supplies of other CIS tobacco in the depressed Russian market. This has been a major blow to the tobacco farmers' income, as the Russian buyers usually paid in advance for up to 95% of the Azeri crop. Trade sources report that, before the crisis, fermented tobacco had sold for \$1.30 to \$1.50 per kilo, and farmers received about \$0.90 per kilo. Since then the price paid to farmers elsewhere in the CIS has fallen to close to \$0.40 per kilo. With the overvalued manat, Azeri farmers are looking to get about \$0.75 per kilo but aren't finding buyers at that price. Fermentation costs about \$0.40 per kilo in Azerbaijan and this pushes the final price too high, to about \$1.35 per kilo when elsewhere in the CIS the price is about \$0.90 per kilo. It remains to be seen if the market will spring back.

Cigarettes

In the cigarette market, the major production plant in Azerbaijan has seen a series of false starts with a revolving cast of ownership partners since 1997, leading to stops and starts in domestic production. Domestic taxation difficulties and other investor uncertainties resulted in a revolving series of international partners in the primary cigarette factory in the country. Since 1997 the Baku Tobacco Company has had American, Turkish, British, and French partners. The first international partner, RJReynolds, contributed the major share in a reported \$35 million investment in a complete refurbishment of the Baku Tobacco Company's plant in 1997 as a joint venture with the Ministry of Agriculture. TEKEL, the Turkish tobacco monopoly, had been one of the first suitors for this J-V, but RJR was able to bring it to fruition. RJR started producing the Astra (Russian) brand and some others, with plans at the time to eventually bring international brands into production. Unfortunately, RJR was overcome by an Azeri excise tax of 45% which strangled the domestic market for legal cigarettes by allowing the much cheaper smuggled cigarettes to capture the market. RJR had engaged the services of Universal Leaf to work with the growers to standardize and improve the tobacco crop, but both companies had left the country by the beginning of 1999. In the meantime, the excise tax has been reduced to 15%, but smuggled cigarettes still are a problem.

RJR sold out its shares in the production plant to a Turkish-Azeri local partner, which attempted to operate the plant but faced insurmountable worker difficulties over back pay issues. After this, a British firm, Sorex Management, won the privatization tender of the plant's joint-stock company. Sorex reportedly got in for a tiny investment of about \$350,000, committed to another \$50 million in upgrades over the next three years, but after six months they too had left, to be replaced by a French organization which has just restarted production this spring.

Under the current circumstances in the market, official and trade statistics for cigarettes are not available to construct accurate production, supply, and demand tables. Trade estimates of local cigarette

production are about 1 billion sticks, with total capacity at approximately 7 to 8 billion sticks per year. Consumption is estimated at 10 to 12 billion sticks per year. Russian, Georgian, and Ukrainian produced cigarettes are imported, along with some legal and many black market international brands. Local and CIS brands sell for \$0.25 to \$0.30 cents a pack of 20 cigarettes, while international brands are sold legally at over \$1.00 a pack and on the black market for just under \$1.00.

With the recent turmoil in the industry, information on every aspect of the tobacco crop and cigarette production is subject to much speculation. The privatization of agriculture in Azerbaijan has left farmers free to respond to market opportunities and they have done so. The lack of income-making opportunities in once-reliable cash crops such as tobacco has pushed many farmers into producing immediately tradable commodities, mostly livestock, fruit, and vegetables. The unpredictability of the tax regime and contract sanctity have made Azerbaijan a difficult market to invest in. The tobacco industry is uncertain in Azerbaijan for the current period and will remain so until general economic conditions allow for the devaluation of the manat and an improvement in the investment climate.

Tobacco Production, Supply, and Demand

PSD Table						
Country	Azerbaijan, Republic of					
Commodity	Tobacco, Unmfg., Total				(HA)(MT)	
	Revised	1998	Preliminary	1999	Forecast	2000
	Old	New	Old	New	Old	New
Market Year Begin		01/1998		01/1999		01/2000
Area Planted	4500	8800	4500	5000	0	3500
Beginning Stocks	7322	0	5822	4000	4322	5300
Farm Sales Weight Prod	10500	15200	10500	8200	0	5740
Dry Weight Production	9000	13700	9000	7400	0	5100
U.S. Leaf Imports	0	0	0	0	0	0
Other Foreign Imports	0	250	0	200	0	200
TOTAL Imports	0	250	0	200	0	200
TOTAL SUPPLY	16322	13950	14822	11600	4322	10600
Exports	8000	8700	8000	5500	0	4000
Dom. Leaf Consumption	2500	1000	2500	600	0	850
U.S. Leaf Dom. Consum.	0	0	0	0	0	0
Other Foreign Consump.	0	250	0	200	0	200
TOTAL Dom. Consumption	2500	1250	2500	800	0	1050
TOTAL Disappearance	10500	9950	10500	6300	0	5050
Ending Stocks	5822	4000	4322	5300	0	5550
TOTAL DISTRIBUTION	16322	13950	14822	11600	0	10600

End of Report.